IN THE

Supreme Court of the United States

October Term, 1973

No. 73-804

GEORGE P. BAKER, RICHARD C. BOND, and JERVIS LANGDON, JR., TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, Debtor,

Petitioners,

v.

GOLD SEAL LIQUORS, INC.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR THE PETITIONERS

PAUL R. DUKE,
JOHN E. WALLACE, JR.,
1138 Six Penn Center,
Philadelphia, Pa. 19104

EDWARD R. GUSTAFSON,
516 West Jackson Boulevard,
Chicago, Illinois 60606

Attorneys for Petitioners

International Printing Co., 711 So. 50th St., Phila., Pa. 19143 — Tel. (215) 727-8711

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OPINIONS BELOW.

The findings of fact and opinion of the District Court for the Northern District of Illinois, entered February 18, 1972, are unreported and are printed in the Single Appendix (A35). The opinion of the Court of Appeals, entered on August 23, 1973 (A38), is reported at 484 F.2d 950.

JURISDICTION.

The judgment of the United States Court of Appeals for the Seventh Circuit was entered on August 23, 1973. A petition for certiorari was filed on November 20, 1973, and was granted January 21, 1974. This Court's jurisdiction rests on 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

Did the court below err in holding that a shipper was entitled to a net judgment and consequently to effect a set-off where a railroad in reorganization sued the shipper for pre-reorganization freight charges and the shipper counter-claimed for pre-reorganization loss and damage to shipments and where the Reorganization Court had denied set-offs to such creditors in the reorganization proceedings.

STATEMENT OF THE CASE

The facts in the case are quite simple. On June 21, 1970, Penn Central Transportation Company filed a petition for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. 205). The petition was filed in the District Court for the Eastern District of Pennsylvania (Reorganization Court), under the caption "In the Matter of Penn Central Transportation Company, Debtor, No. 70-347," and on the same day the Reorganization Court entered Order No. 1 approving the petition. Paragraph 10 of Order No. 1 provided:

> "10. All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, against any obligation of the Debtor until further order of this Court." (A31-32)

On July 22, 1970, pursuant to Court Order No. 20, George P. Baker, Richard C. Bond, Jervis Langdon, Jr., and Willard Wirtz were appointed Trustees of the Debtor. The Trustees, *inter alia,* sought, as authorized by paragraph 5 of Order No. 1 (A29-30), to collect the assets of the Debtor's estate, of which one was a claim for freight charges which Gold Seal Liquors owed to the Debtor.

On December 22, 1970, the Trustees brought suit in the United States District Court for the Northern District of Illinois against Gold Seal Liquors to recover $8,256.61 in freight charges which had accrued during a period of approximately a year and a half prior to June 21, 1970 (A4).

The cause of action arose under the laws of the United States regulating commerce, 49 U.S.C. Sections 3(2) and 6(7), and the District Court below had jurisdiction of the action under 28 U.S.C. Section 1337. Gold Seal Liquors filed a counterclaim for $19,319.42 for loss and damage to various shipments accruing over a period of approximately two years prior to June 21, 1970 (A7-8).

The parties filed a stipulation of facts in which Gold Seal Liquors admitted its liability to the Trustees in the amount of $6,999.76, and the Trustees acknowledged their liability to Gold Seal Liquors in the amount of $18,016.77 (A11-14). The Trustees filed a motion for summary judgment which prayed that the Court enter a judgment for plaintiff in the amount admitted by defendant, Gold Seal, and for defendant in the amount admitted by the plaintiff Trustees (A17-18).

Previous to the institution of this action, the Reorganization Court had prohibited various bank creditors from offsetting against the Debtor (*Penn Central Transportation Co. v. National City Bank of Cleveland, et al.*, 315 F. Supp. 1281 (E.D. Pa. 1970) (Bank Setoff Case)), and had under advisement a petition of the Trustees for an order directing certain shippers to pay amounts due Debtor and prohibiting the shippers from offsetting.

After the institution of this matter, but prior to a decision by the Illinois District Court, the *Bank Setoff Case* was affirmed by the Third Circuit Court of Appeals. *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *cert. den.* 408 U.S. 923 (1972). Further, during the same period, the Reorganization Court entered Order No. 571 granting the Trustees' petition prohibiting certain shippers, *inter alia*, from setting off freight loss and damage claims against amounts owed the Debtor for freight transportation services. *In the Matter of Penn Central Transportation Company, Debtor*, 339 F. Supp. 603 (1972),

aff'd. 477 F.2d 841 (3d Cir. 1973), *cert. den.* — U.S. — (No. 72-1698, 42 U.S. Law Week 3213); *aff'd. sub nom. U.S. Steel Corp. v. Trustees,* — U.S. — (No. 73-94, 42 U.S. Law Week 3213) (Shippers' Setoff Case).

The Illinois District Court granted plaintiff Trustees' motion for summary judgment, but set off one judgment against the other, which resulted in a net judgment in favor of Gold Seal Liquors against the Trustees in the amount of $11,017.01. The Court stated that restraints of setoffs by the Reorganization Court were only against extra-judicial self-help setoffs, and that in the matter before it, denial of the setoff would be inequitable (A37).

The Trustees appealed. The Circuit Court affirmed. Affirmance for the net judgment permitted Gold Seal Liquors to recover dollar for dollar on its pre-reorganization claim for loss and damage to the extent of the amount of the Trustees' admitted claim against Gold Seal, *viz.*, $6,999.76.[1]

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1. Although the Circuit Court stated that Gold Seal Liquors must now submit its claim on the judgment to the Reorganization Court, it has, by affirming the net judgment, already permitted Gold Seal Liquors to recover $6,999.76.

ARGUMENT I

THE DISTRICT COURT HANDLING THE REORGANIZATION OF THE DEBTOR HAS EXCLUSIVE JURISDICTION OVER THE PROPERTY OF THE DEBTOR AND THEREFORE THE COURT BELOW ERRED IN ENTERING A NET JUDGMENT THEREBY DISPOSING OF PETITIONERS' CHOSE IN ACTION.

Section 77(a) of the Bankruptcy Act provides in pertinent part:

> "If the petition is so approved, the court in which the order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have *exclusive jurisdiction of the debtor and its property wherever located* . . . ." [Emphasis added.]

Upon approving Penn Central Transportation Company's (Debtor) petition for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. Section 205), the Reorganization Court became vested with exclusive jurisdiction over the property of the Debtor. *In re New York, New Haven and Hartford Railroad Co.*, 457 F.2d 683 (2d Cir. 1972) *cert. den.* 409 U.S. 890 (1972); *Calloway v. Benton*, 336 U.S. 132, 147 (1949); *Ex Parte Baldwin*, 291 U.S. 610.

In *Ex Parte Baldwin*, 291 U.S. 610, 615 (1934), this Honorable Court stated:

> "All property in the possession of a bankrupt of which he claims the ownership passes, upon the filing of a petition in bankruptcy, into the custody of the court in bankruptcy. . . . Having possession, the Court may not only issue all writs necessary to protect its possession from physical interference, but is entitled to determine all questions respecting the same . . . ."

In the exercise of its exclusive jurisdiction over the property of the Debtor, the Reorganization Court entered Order No. 1 which, *inter alia*, enjoins setoffs (A31-32).[2] The setoff provisions of Order No. 1 were first tested in the *Bank Setoff Case* which was affirmed by the Third Circuit Court of Appeals. *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *cert. den.* 408 U.S. 923 (1972).

Subsequent to the *Bank Setoff Case*, in the *Shippers' Setoff Case* (339 F. Supp. 603), the Trustees petitioned the Reorganization Court for an order directing numerous shippers to pay several million dollars in freight charges due the Debtor.[3] These creditors had refused to pay the freight charges except to the extent a balance might be left after they had offset against the freight charges amounts which they claimed the Debtor owed them. The Reorganization Court first concluded that the Debtor had an obligation to collect freight charges due it, and the existence of claims against the Debtor did not change this. That Court then recognized that, but for reorganization, the shippers' claims against the Debtor could be litigated in actions brought by the Debtor to collect its freight charges. Noting that the Third Circuit Court of Appeals in the *Bank Setoff Case, supra*, had affirmed the Reorganization Court's jurisdiction to control the exercise of setoff rights, the Reorganization

2. While a setoff or counterclaim is automatically permitted in an ordinary bankruptcy because of Section 68 of the Bankruptcy Act (11 U.S.C. § 108), it is not mandatory in reorganizations. *Susquehanna Chemical Corporation v. Producer's Bank & Trust Co.*, 174 F.2d 783 (3d Cir. 1949); *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *In the Matter of Penn Central Transportation Co.*, 477 F.2d 841 (3d Cir. 1973); see also *Lowden v. N.W. National Bank*, 298 U.S. 160 (1936); *In re Lehigh and Hudson River Ry. Co.*, 468 F.2d 430, 433 (2d Cir. 1972).

3. Respondent was not a party to this petition and the Trustees do not contend he is in violation of the Court's specific order emanating from the petition.

Court proceeded to answer the question of whether the Court should exercise its discretion to enjoin setoffs in the circumstances presented.

The Court reviewed the relevant factors and concluded that setoffs should not be permitted at this time. The relevant factors were as follows:

> 1. to permit the setoffs would be to discriminate against the vast majority of shippers who had paid their pre-bankruptcy freight charges in full;
>
> 2. the cash need of the reorganization must be considered. It is more consistent with the overall purposes of Section 77 of the Bankruptcy Act that shipper claims be disposed of in the proofs of claim procedure rather than that current operating revenues of the Debtor should be jeopardized by setoffs; and
>
> 3. the Trustees, in the exercise of their business judgment, in an attempt to treat all parties fairly, requested that setoffs be restrained (339 F. Supp. 603, 608 (E.D. Pa. 1972)).

The Third Circuit Court of Appeals affirmed the summary jurisdiction of the Reorganization Court and reiterated that it was in that Court's sound discretion to determine "whether or not to permit setoff or counterclaim against the Debtor's charges." (477 F.2d at 845).[4]

Despite the denial of setoffs by the Reorganization Court, and despite its exclusive jurisdiction over the property of the Debtor, the Court of Appeals for the Seventh Circuit, by affirming the entry of a net judgment in this matter, has disposed of property of the estate, *viz.*, an admittedly valid chose in action for $6,999.76. It has required it to be applied in partial payment of a pre-reorgan-

4. In two separate efforts to obtain review of this matter, this Court affirmed summarily and denied certiorari. See pp. 4-5, *supra*.

ination claim against the estate of the Debtor for loss or damage to freight.[5]

This was clearly erroneous. The Reorganization Court has exclusive jurisdiction over the property of the Debtor, including the $6,999.76. The court below lacked power to dispose of this property. In entering the net judgment instead of granting the relief prayed for by the Trustees and entering separate judgments on petitioners' claim and respondent's counterclaim, the court below erred. The Seventh Circuit belatedly recognized that the "judgment of the Illinois court must now be submitted to the reorganization court with all other claims, to be satisfied in accordance with the appropriate orders of that court." (A40-41). However, this recognition only partially accedes to the jurisdiction of the Reorganization Court, for having affirmed the entry of a *net* judgment, it has *pro tanto* interfered with property in the exclusive possession of that Court.

The proper procedure that the courts below should have employed is evidenced in a case similar to the instant one and involving petitioners, *i.e., Trustees v. Southeastern Michigan Shippers Co-Operative Association* (B1).[6] Here also both parties were indebted to one another, and one of the issues was whether setoff should be permitted. The Court analyzed the setoff issue thoroughly and concluded that ". . . this court is without power to effect a set-off

5. The Trustees do not contend that the court below lacked jurisdiction to decide the counterclaim to the extent of liquidating the claim. Section 77(j) provides that "suits or claims for damages caused by the operation of trains, . . . may be filed and prosecuted to judgment in any court of competent jurisdiction. . . ." See *Liquid Carbonic Corp. v. Erie R. Co.*, 171 Misc. 969, 14 N.Y.S. 2d 168 (1939); *Erie R. Co. v. Wm. J. Pfeil, Inc.*, 256 App. Div. 465, 11 N.Y.S. 2d 155 (1939).

6. The decision is as yet unreported. It is printed in an Addendum to this brief as a convenience for the Court and cited herein as "(B—)."

of any amounts recovered. . . ." (B15). Pursuant to Section 77(j) of the Bankruptcy Act, and in the interest of judicial economy, the Michigan District Court has permitted the counterclaim to be prosecuted and, if successful, has required that it be presented to the Reorganization Court for proof and allowance. In this regard the Michigan District Court stated:

> "In essence, the bankruptcy court may modify in any way it feels necessary any right asserted against the debtor which might adversely affect the reorganization plan. The fact that it is raised in the form of a counterclaim to a suit instituted by the trustees is irrelevant. The counterclaim is not a defense to the original claim, but an independent claim which must be approached on its own merits." (footnote omitted) (B8).

The Illinois District Court failed to recognize this distinction and erred in entering net judgments. As the Michigan District Court stated:

> "Even if this court may also hear defendant's counterclaim . . . , it may not satisfy that judgment out of the debtor's property, including its judgment in this suit. Once 'the claim is reduced to judgment [it] may then be presented to the bankruptcy court for proof and allowance.' *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946)." (B8).

This procedure followed by the Michigan Court accords full deference to the exclusive jurisdiction of the Reorganization Court, but at the same time is consistent with the dictates of judicial economy and efficiency. It permits liquidation of the two claims in the proceedings before it, but does not dispose of any property of the Debtor's Trustees or make any payment on claims which are within the exclusive jurisdiction of the Reorganization Court.

ARGUMENT II

IF ALLOWED TO STAND THE DECISION OF THE COURT BELOW WOULD HAVE A SERIOUS DETRIMENTAL EFFECT ON THE REORGANIZATION OF THE DEBTOR AND WOULD PERMIT INEQUITABLE TREATMENT OF CREDITORS OF THE SAME RANK.

While the amount involved in this one proceeding is relatively small, there are several other suits pending in courts in the Seventh Circuit which would obviously be governed by the decision below and, unless overturned, will result in claimants who happened to be sued in that Circuit receiving a clear preference over all other claimants with similar claims. As indicated above, considerations of practicality and judicial economy are what compelled the Trustees to liquidate their own claim in the District Court for the Northern District of Illinois. As shown by the record herein, there was a dispute as to the actual amount owing to the Trustees on their chose in action for freight charges, and it was not until the factual dispute was resolved (here admittedly by way of stipulation) that the actual amount of the chose was liquidated. In a reorganization proceeding of this magnitude, to compel the Trustees to recover on every chose in their possession in the Reorganization Court could bring the reorganization proceeding itself to a standstill.

By failing to consider properly the reorganization proceeding of the Debtor, the courts below have discriminated in favor of Gold Seal Liquors to the detriment of other creditors of the Debtor. Other loss and damage claimants are relegated to the proof of claim procedure to recover any amounts owed to them. The judgment below is grossly unfair in that it permits Gold Seal Liquors to recover

presently at least the amount of the setoff, $6,999.76, 100 cents on the dollar. If the holding below is permitted to stand, the Trustees will be faced with a Hobson's choice. They will have to forego the attempt to recover property of the estate in other fora, which is inconsistent with principles of judicial economy and efficiency, or prosecute such actions, with the result that certain creditors will recover all or part of their pre-bankruptcy claims, while other creditors are denied that right.

It should be noted that the Reorganization Court, in denying the right of setoff, stated that such denial would be "without prejudice to the recognition of the appropriate priority of such claims in the ultimate reorganization of the Debtor" (339 F. Supp. at 606.) Thus the Reorganization Court has attempted to accommodate the needs of the Debtor in the reorganization with the claims of the creditors who are denied the right of setoff.

CONCLUSION

The decision below should be reversed with the direction that separate judgments be entered on petitioners' claim and respondent's counterclaim.

Respectfully submitted,

PAUL R. DUKE,
JOHN E. WALLACE, JR.,
1138 Six Penn Center
Philadelphia, Pa. 19104
EDWARD R. GUSTAFSON,
516 W. Jackson Boulevard
Chicago, Illinois 60606
Attorneys for Petitioners

ADDENDUM.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION.

Civil Action
No. 39090.

GEORGE P. BAKER, RICHARD C. BOND, JERVIS LANGDON, JR., AND WILLARD WIRTZ, TRUSTEES OF THE PROPERTY OF PENN CENTRAL TRANSPORTATION COMPANY, A PENNSYLVANIA CORPORATION, DEBTOR,

Plaintiffs,

v.

SOUTHEASTERN MICHIGAN SHIPPERS CO-OPERATIVE ASSOCIATION, A/K/A SEMCO, INC., A MICHIGAN CORPORATION,

Defendant.

Memorandum Opinion.

(Filed September 28, 1973.)

Plaintiffs (trustees of the property of Penn Central Transportation Company) sue for freight charges totaling $22,773.19 incurred by defendant (SEMCO, Inc.) between October 10, 1969, and November 11, 1969. Defendant pleads a prior accord and satisfaction and, in the alternative, counterclaims against plaintiffs in the amount of $20,179.80 for damages to cargo sustained on February 21, 1969, and March 3, 1969. It is these damage claims which defendant

contends were previously set off against the freight charges now sought by plaintiffs, the difference of $1,852.07 having been tendered and accepted on November 17, 1969.

Accord and Satisfaction.

It appears that SEMCO did try to arrange a mutual cancellation of accounts—the railroad's carriage charges against the shipper's claims for damages to cargo. Based on the facts elicited on these cross-motions for summary judgment, however, it is unclear whether these efforts came to a legally effective fruition.[1] There are genuine and material issues of fact yet to be decided on this question, and if there were no other factors involved, this case would be inappropriate for summary disposition. This result is complicated and somewhat altered by two additional facts: (1) the freight charges involved here are covered by the Interstate Commerce Act[2] and (2) since these claims accrued

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1. "We recognize the Michigan rule that to constitute an accord and satisfaction, the tender of payment as being in full should be made in unequivocal terms so that the creditor in accepting the payment will do so understandingly. Durkin v. Everhot Heater Co., 266 Mich. 508, 513, 254 N.W. 187 [1934]." Allstate Ins. Co. v. Springer, 269 F.2d 805, 809 (6th Cir. 1959), cert. denied, 361 U.S. 932 (1960). See also Lafferty v. Cole, 339 Mich. 223, 228 (1954) (creditor must be "fully informed of the condition accompanying acceptance"). This is merely a corollary to the general principle that an accord requires a meeting of the minds of the parties in an agreement to substitute one type of performance for another. See Stadler v. Ciprian, 265 Mich. 252, 262 (1933).

Here the evidence indicates that defendant's offer of settlement was ambiguous and equivocal. In a letter dated November 19, 1969, defendant's executive manager indicated that the off-setting of accounts and payment of the difference did not mean that SEMCO was declining payment of the freight charges, but that they would be paid as soon as the damage claims were approved by the railroad. Without further proof of the parties' intentions, this is insufficient to prove the existince (or nonexistence) of the claimed accord.

2. 49 U.S.C. § 1 *et seq.*

the railroad has entered into reorganization under the Bankruptcy Act.[3]

First, plaintiffs argue that whether or not the facts make out an accord and satisfaction is in the end irrelevant, for Section 6(7) of the Interstate Commerce Act[4] absolutely prohibits and nullifies such arrangements. That section, prompted by a congressional purpose to eliminate secret preferences and kickbacks to shippers,[5] mandates strict adherence to published tariffs.[6] In applying this provision, the Supreme Court has held that a carrier may be compensated for its services only by payment in cash[7]

3. Reorganization of the Penn Central Transportation Company under 11 U.S.C. § 205 was initiated by an order of the District Court for the Eastern District of Pennsylvania on June 21, 1970 [hereinafter cited as Order No. 1], approving the railroad's petition and containing various provisions concerning its continued operation. Relevant materials may be found in the Corporate Reorganization Reporter (Penn Central).

4. "No carrier, unless otherwise provided by this chapter, shall engage or participate in the transportation of passengers or property, as defined in this chapter, unless the rates, fares, and charges which the same are transported by said carrier have been filed and published in accordance with the provisions of this chapter; nor shall any carrier charge or demand or collect or receive a greater or less or different compensation for such transportation of passengers or property, or for any service in connection therewith, between the points named in such tariffs than the rates, fares, and charges which are specified in the tariff filed and in effect at the time; nor shall any carrier refund or remit in any manner or by any device any portion of the rates, fares, and charges so specified, nor extend to any shipper or person any privileges or facilities in the transportation of passengers or property, except such as are specified in such tariffs." 49 U.S.C. § 6(7).

5. See, e.g., Atchison, T. & S.F. Ry. Co. v. Bouziden, 307 F.2d 230, 234 (10th Cir. 1962); Baker v. Prolerized Chicago Corp., 335 F. Supp. 183, 185 (N.D. Ill. 1971). See also 49 U.S.C. § 3(1) (prohibiting preferences or prejudices).

6. "The lawful rate is that which the carrier *must* exact and that which the shipper *must* pay." Kansas City So. Ry. Co. v. Carl, 227 U.S. 639, 653 (1913) (emphasis added).

7. Louisville & N.R. Co. v. Mottley, 219 U.S. 467, 477 (1911).

or by check [8] or by way of judicial set-off against judgments due the shipper.[9] Any form of payment containing the potential for departure from the exact letter of the tariffs (such as the supplying of goods and services in exchange for carriage) [10] is prohibited.

Defendant argues that the exception for judicial set-offs, enunciated by the Court in *Chicago & N.W. Ry. Co. v. Lindell*, 281 U.S. 14 (1930), should be extended to a prior set-off of accounts (rather than judgments) concluded informally between the parties. Defendant cites no cases supporting this position. *Burlington Northern Inc. v. United States*, 462 F.2d 526 (Ct. Cl. 1972), falls squarely within the *Lindell* exception. "According to plaintiff's reading, there can be no deduction of a damage claim against transportation charges except by adjudication of a court. But that is exactly the situation we have here." 462 F.2d at 529. The same is true of *Yale Express System, Inc. v. Nogg*, 362 F.2d 111 (2nd Cir. 1966), and *Southern Pacific Co. v. Miller Abattoir Co.*, 454 F.2d 357 (3rd Cir. 1972).

On the other hand, at least two courts have squarely faced the issue of whether non-judicial set-offs are permissible under the Interstate Commerce Act, and have determined that they are not.

> "Another group of shippers contend that, prior to bankruptcy, there was an agreed settlement of mutual accounts between the Debtor and the shipper, with the result that the Debtor either owes money to the shippers, or is owed much less than is now being claimed by the Trustees. . . . To the extent that the Debtor's

8. Fullerton Lumber Co. v. Chicago, M., St. P. & P.R. Co., 282 U.S. 520, 522 (1931).

9. Chicago & N.W. Ry. Co. v. Lindell, 281 U.S. 14, 17 (1930).

10. Chicago, I. & L. Ry. Co. v. United States, 219 U.S. 486, 496-97 (1911).

claims against these companies were based on freight charges, it is clear under the principles set forth previously that they were incapable of being discharged either by unilateral set-offs or by mutual agreement." *In re Penn Central Transportation Co.*, 339 F. Supp. 603, 607 (E.D. Pa. 1972).

This conclusion was specifically approved by the Third Circuit:

> "[One of the appellants] contends that under applicable Pennsylvania law, it extinguished its debt to the railroad by the nonjudicial set-off of a debt owed to it by the carrier . . . . Even assuming the validity of appellant's contention under Pennsylvania law, such a set-off would have been in express contravention of the Interstate Commerce Act. Indeed, the Act was so designed to prevent the kind of secret kickbacks which this type of practice could lead to." *In re Penn Central Transportation Co.*, 477 F.2d 841, 845 (3rd Cir. 1973).

The reason for distinguishing between judicial and nonjudicial set-offs is obvious. In the former case, there is no adjustment until the exact value of each party's claim has been authoritatively determined; in the latter instance, there is no guarantee that the debt off-set against the freight charges is worth the amount allowed. When the set-off is judicially supervised, there is little opportunity for collusion; when it is privately arranged, there is no such assurance. In short, it is the policy of the Act to permit payment of freight charges only in a manner offering little or no opportunity for evasion of the tariff. Judicial set-offs satisfy this requirement while private arrangements do not.

As a result, the accord and satisfaction pleaded by defendant, even if convincingly established, is inadequate to

resist the trustees' cause of action. Because defendant interposes no other defenses,[11] plaintiffs are entitled to summary judgment for the undisputed portion of their claim—$22,039.89—minus the $1,852.07 previously paid. There is a genuine dispute of fact as to waybills 223588 and 228460, totaling $733.32, which must be resolved at trial.

The Counterclaim.

The railroad's reorganization raises a second question, namely whether the defendant may nevertheless recover in this court on its counterclaim. Initially, it should be noted that its claim is contested, both as to liability and damages. There has been presented no evidence from which this court can decide the issues raised, and therefore the defendant's cross-motion for summary judgment must be denied in any event.

Under *Lindell*, this court would ordinarily be authorized to proceed to judgment on the conterclaim and off-set any recovery thereunder against plaintiff's recovery. The problem is to determine what effect the intervening reorganization may have on the defendant's cause of action. Two issues must be considered: (1) whether the action may be maintained in this court and (2) if so, whether this court is empowered to set off any recovery against that of plaintiff (*i.e.*, in effect to execute upon the judgment).

1. *Set-off.* Taking the second point first, this court is immediately confronted with 11 U.S.C. § 205(a), which gives the bankruptcy court in a railroad reorganization "exclusive jurisdiction of the debtor and its property wherever located . . . ." "Property" in the bankruptcy setting includes a cause of action such as that asserted by

11. "The Consignee alleged the Railroad's breach both as a defense and as a counterclaim. The alleged breach, however, does not constitute a defense to the Railroad's claim for freight charges, but constitutes an independent claim. . . ." Southern Pacific Co. v. Miller Abattoir Co., 454 F.2d 357, 362 (3rd Cir. 1972).

the trustees in this case [12] and any recovery granted thereunder.[13] "Exclusive jurisdiction" is generally given a literal interpretation.[14] It follows that this court can exercise jurisdiction over the bankrupt's property, including a judgment or cause of action, only to the extent permitted by the bankruptcy court.[15]

That court, by its order of June 21, 1970, has authorized the trustees to institute and prosecute in any court suits for the recovery or protection of its property or rights,[16] and to settle or defend claims against the debtor,[17] including, in their discretion, "claims for loss, damage or delay to freight and baggage . . . ." [18]

> "[B]ut no payment shall, without further order of this Court, be made by the Debtor in respect of any such actions, proceedings or suits on claims accruing prior to the date of this order except such claims as may be permitted to be paid by this order or by other general orders hereafter entered herein, and such as constitute preferred claims under the Acts of Congress relating to bankruptcy; and no action taken by the Debtor in defense or settlement of such claims, actions, proceedings, or suits shall have the effect of establishing any claim upon, or right in, the property or funds in the possession of the Debtor that otherwise would not exist." [19]

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12. 11 U.S.C. § 110(a)(6).

13. Meyer v. Fleming, 327 U.S. 161, 165 (1946).

14. See, e.g., In re New York N.H. & H.R. Co., 457 F.2d 683, 689 (2nd Cir. 1972); In re Imperial "400" National, Inc., 429 F.2d 671, 676-77 (3rd Cir. 1970).

15. Cf. Warren v. Palmer, 310 U.S. 132 (1940); Ex parte Baldwin, 291 U.S. 610 (1934).

16. Order No. 1, *supra*, note 3, ¶ 5.

17. *Id.*

18. *Id.*, ¶ 3B.

19. *Id.*, ¶ 5.

Thus, it appears that this court is empowered to adjudicate the plaintiffs' claim, but that it has no authority to dispose of any recovery upon that claim, whether by way of set-off or otherwise. Even if this court may also hear defendant's counterclaim (a matter yet to be decided), it may not satisfy that judgment out of the debtor's property, including its judgment in this suit. Once "the claim is reduced to judgment [it] may then be presented to the bankruptcy court for proof and allowance." *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946).

2. *Authority to Entertain Counterclaim.* The bankruptcy court has exclusive jurisdiction over not only the debtor's property, but over "any rights that may be asserted against it. These rights may be altered in any way thought necessary to achieve sound financial and operating conditions for the reorganized company, subject to the requirements of the Act." *Callaway v. Benton*, 336 U.S. 132, 147 (1949). In a railroad reorganization the class of claims included within the scope of this power is very great. "The term 'claims' includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character." 11 U.S.C. § 205(b).[20]

In essence, the bankruptcy court may modify in any way it feels necessary any right asserted against the debtor which might adversely affect the reorganization plan. The fact that it is raised in the form of a counterclaim to a suit instituted by the trustees is irrelevant. The counterclaim is not a defense to the original claim, but an independent claim which must be approached on its own merits.[21]

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20. Also, cf. 11 U.S.C. § 205(b): "The term 'creditors' shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act. . . ."

21. See note 11, *supra*.

11 U.S.C. § 108, authorizing certain set-offs and counterclaims in ordinary bankruptcy, is not binding in Chapter X corporate reorganization cases, where it could defeat the very purpose of the reorganization by depriving the debtor corporation of much-needed working capital, thus endangering its ability to continue in operation.[22] In railroad reorganizations, where the public interest in survival of the enterprise is even more compelling, the reorganization court may not only enjoin set-offs,[23] but may go further and

> ". . . enjoin or stay the commencement or continuation of suits against the debtor until after final decree; and may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree: *Provided,* That suits or claims for damage caused by the operation of trains, busses, or other means of transportation may be filed and prosecuted to judgment in any court of competent jurisdiction and any order staying the prosecution of any such cause of action or appeal shall be vacated." 11 U.S.C. § 205(j).

The Penn Central reorganization court has enjoined certain set-offs,[24] which the parties seem to have assumed

22. Lowden v. Northwestern National Bank, 298 U.S. 160, 163-66 (1936); In re Yale Express System, 362 F.2d 111, 116-17 (2nd Cir. 1966); Susquehanna Chemical Corp. v. Producers Bank & Trust Co., 174 F.2d 783, 787 (3rd Cir. 1949).

23. Penn Central Transportation Co. v. National City Bank of Cleveland, 315 F. Supp. 1281, 1283-84 (E.D. Pa. 1970), affirmed sub nom. In re Penn Central Transportation Co., 453 F.2d 520, 522-23 (3rd Cir. 1972).

24. "All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined

are applicable in this case, though the assumption is a rather questionable one. This point is mooted, however, by the court's broader command that:

> "All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnisheeing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion or the assets, goods, money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction . . . ."[25]

Because of the bankruptcy court's exclusive jurisdiction over such matters, that mandate is binding upon this court.

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24. (Cont'd.)
from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, [sic] against any obligation of the Debtor, until further order of this Court." Order No. 1, *supra* note 3, ¶ 10 (footnote omitted).

25. *Id.*, ¶ 9.

Thus the ultimate issue is whether the proviso in subsection (j) of the statute, incorporated verbatim in the court's order, applies to defendant's counterclaim. If it constitutes a claim "for damages caused by the operation of trains, busses, or other means of transportation," it is cognizable in this court. If not, it falls within the scope of the order and its prosecution here is effectively enjoined.

There is relatively little case law interpreting the proviso, and what there is is either contradictory or inconclusive. Certainly "[t]he language of the proviso in § 77(j) is sufficiently broad to include all tort or contract claims whatsoever that arise from the operation of the trains or busses of the debtor." 5 *Collier on Bankruptcy* ¶ 77.12 at 516 (14th ed. 1970). Such a literal reading of the statute would clearly place SEMCO's counterclaim within the proviso. On their facts, several cases from the New York courts appear to support this result. See *Erie R. Co. v. William J. Pfeil, Inc.*, 11 N.Y.S.2d 155, 256 App. Div. 465 (1939) (counterclaim for damage to shipment of beans caused by salt in car held to be within proviso; counterclaim for breach of contract to construct a side track was outside proviso); *Yerckes-Eichenbaum, Inc. v. McCarthy*, 35 N.Y.S.2d 527, 264 App. Div. 403 (1942) (action for breach of contract of carriage within proviso); *Liquid Carbonic Corporation v. Erie R. Co.*, 14 N.Y.S.2d 168, 171 Misc. 969 (1939) (damage to cargo caused by failure to provide proper unloading facilities held to be within proviso). On the other hand, an opinion of the Seventh Circuit Court of Appeals of about the same vintage discusses the proviso at length, and concludes that Congress intended only to exempt personal injury claims. *In re Chicago & E. I. Ry. Co.*, 121 F.2d 785, 789 (7th Cir. 1941), *cert. denied sub nom. Chicago & E. I. Ry. Co. v. Gourley*, 314 U.S. 653 (1941). Two other federal courts have effectively avoided the issue in personal injury cases, which are uniformly recognized as

falling within the proviso. *Munnelly v. Farrell*, 317 F. Supp. 329 (S.D.N.Y. 1970); *Rodabaugh v. Denny*, 24 F. Supp. 1011 (S.D.N.Y. 1938). Finally, one other federal court seemed in passing to endorse the personal injury restriction, but went on to hold that a penalty for violation of the Safety Appliance Act is outside the proviso without ever defining its exact scope. *United States v. Dorigan*, 236 F. Supp. 106, 108 (E.D.N.Y. 1964).

It seems a sound rule of construction to adopt the simplest, most obvious interpretation of statutory language, unless there are clearly shown, persuasive reasons for doing otherwise.[26] A court may reasonably adopt a narrower or broader construction when to do so would better effectuate legislative intent.[27] This imperfectly expressed intent may have been actual (often discovered in legislative history) or it may be implied (a euphemism for the judicial rounding off of a law's sharp corners). But however the burden of justifying a non-literal interpretation is formulated, it has not been satisfied here. There is no legislative history to indicate that Congress intended something other than what it appeared to say. There is no evidence of overriding policies or dysfunctional effects which would permit this court to conclude that Congress should or would have intended something else, and to impute to it such intent *nunc pro tunc*.

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26. "True, courts in the interpretation of a statute have some scope for adopting a restricted rather than a liberal or a usual meaning of its words where acceptance of that meaning would lead to absurd results, . . . or would thwart the obvious purpose of the statute. . . . But courts are not free to reject that meaning where no such consequences follow and where, as here, it appears to be consonant with the purposes of the Act as declared by Congress and plainly disclosed by its structure." Helvring v. Hammel, 311 U.S. 504, 510-11 (1941).

27. "It is well established, however, that a meaning not conveyed by the literal language may be given in order to carry out the legislative intention, if the words used will bear such meaning." United States v. Breenan, 214 F.2d 268, 270 (D.C. Cir. 1954), cert. denied, 348 U.S. 830 (1954).

Indeed, to the extent there are such factors, they weigh in favor of a literal reading of the proviso. First, it would not alter the bankruptcy court's power to rule on the allowance of such claims, thus producing no interference with any part of the reorganization plan (which is the primary *raison d'être* for this section of the statute).

Second, the policy behind the subsection (j) proviso itself appears to be similar to that behind 28 U.S.C. § 959, permitting suit without leave of the bankruptcy court respecting acts or transactions of the trustees in "carrying on" the debtor's business. Referring to a predecessor of that section, the Supreme Court observed that:

> "This act abrogated the rule that a receiver could not be sued without leave of the court appointing him, and gave the citizen the unconditional right to bring his action in the local courts, and to have the justice and amount of his demand determined by the verdict of a jury. He ceased to be compelled to litigate at a distance, or in any other forum, or according to any other course of justice, than he would be entitled to if the property or business were not being administered by the Federal court.
>
> "The object of the section is manifest, and it is equally plain that that object would be open to be defeated if the receiver could remove the case at his volition. The intention to permit this to be done cannot reasonably be imputed to Congress, and, moreover, such a right would be inconsistent with the general policy of the act." *Gableman v. Peoria, D. & E. Ry. Co.*, 179 U.S. 335, 338 (1900).

Such a rationale suggests no basis for distinguishing between claims for property damage and those for personal injury. Judge Patterson, in the *Rodabaugh* case, reached a similar conclusion in an analogous situation:

"In a very broad sense every action against a railroad company wherein money damages are demanded is an action for 'damages caused by the operation of trains, busses, or other means of transportation.' The primary business of a railroad company is to operate trains, and all its activities are incidental to the operation of trains. The words of the proviso are not to be construed so broadly; nor on the other hand, should they be construed so narrowly as to defeat the purpose of Congress in enacting the proviso. Congress doubtless had in mind the fact that the district court in charge of reorganization might be a long distance from the court in which an action for damages might be brought, and that the obtaining of consent of the court in charge of reorganization might be a hardship on a claimant. This is a factor in favor of a liberal interpretation of the proviso. There is no apparent reason for a distinction between the case of a plaintiff who is struck by a moving train and the case of a plaintiff who was injured by the collapse of a scaffold while working as an employee of the railroad. I am of opinion [sic] that the present case is one 'for damages caused by the operation of trains, busses or other means of transportation' and that the prosecution of the action in the usual manner has not been restrained by the reorganization court." 24 F. Supp. at 1012.

Finally, it must be remembered that defendant presses its claim in this court only in response to one initiated here by the trustees themselves. To hear the plaintiffs' case but not the defendant's, when both might easily be disposed of in one action, seems not only an uneconomic allocation of judicial resources but also an unduly harsh and useless result. As a general rule, statutes should be construed so

as to avoid the imposition of such arbitrary and meaningless hardships.[28]

For these reasons, summary judgment will enter in favor of plaintiffs for the undisputed portion of their claim. The remainder of their claim, as well as defendant's counterclaim, may be prosecuted in this court. However, this court is without power to effect a set-off of any amounts recovered pursuant thereto.

An appropriate order may be submitted.

JOHN FEIKENS,
United States District Judge.

DATED: DETROIT, MICHIGAN
SEPTEMBER 28, 1973.

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28. "The courts draw back from the construction of an ambiguous statute that would lead to unjust results, just as nature draws back from the consistency of one of its laws that would encase in ice fish at the bottom of a river." Voris v. Gulf-Tide Stevedores, 211 F.2d 549, 552-53 (5th Cir. 1954), cert. denied, 348 U.S. 823 (1954).